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Investment Treaty News Quarterly is published by
The International Institute for Sustainable Development
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9, Chemin de Balexert, 5th Floor
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Only a Brief Pause for Breath: The Judgment of the German Federal Constitutional Court on CETA

Jelena Bäumler



On October 13, 2016, the German Federal Constitutional Court (FCC) issued its much-awaited judgment on the request for temporary legal protection against the Canada–European Union Comprehensive Economic and Trade Agreement (CETA). The Court delivered a Solomonic, but somehow puzzling judgment.

1. The content of the judgment

First, it should be stressed that this is not the final judgment on the matter, but a judgment on a request for temporary injunction on the basis that irreversible damages might occur in case measures were not issued by the court. The complainants argued in essence that a positive decision by the European Union and its member states to sign and provisionally apply CETA would violate their rights under the German Constitution (namely Art. 38(1) in connection with Art. 79(3) and Art. 20(1) and (2)). The complainants (altogether more than 125,000—among whom the left-wing party Die Linke, consumer protection organizations and an individual flute teacher—combined in one proceeding) pledged the Court to disallow the German member to approve CETA in the European Council voting.

The Court rejected the claim. Yet, it delivered one of its famous “yes, but...” judgments. The FCC decided that the German representative may agree to CETA in the Council—in the Court’s view, requiring unanimous voting, which in itself is not undisputed among EU law experts—but only if the following three conditions are met:

1. Any Council decision regarding CETA must only concern those parts of the agreement that fall within the exclusive competence of the European Union.
2. Until the final judgement of the FCC, the Court requires sufficient “democratic backing” of any decision taken by the committees to be established under CETA.
3. CETA Art. 30.7(3)(c) has to be interpreted as to allow Germany to unilaterally terminate the provisional application of CETA.

In its reasoning, the Court emphasized that a decision on temporary relief requires careful weighing of the detrimental effects for the complainants *without* any preliminary measures issued by the Court and the consequences *if* the Court ordered the government to disapprove CETA in the Council voting. The Court reasoned that, on the one hand, the restrictions on the German government to develop and to actively participate in EU foreign and trade policy as well as the detrimental consequences for the European Union as a whole to negotiate and conclude trade agreements could be immense. A negative vote of the German representative in the Council on the signing and provisional application could in fact be irreversible and most probably effectively lead to the death of CETA, thereby seriously damaging the reputation and trust in the reliability of Germany as well as the European Union. On the other hand, the consequences of an affirmative vote could lead to the provisional application of CETA, but—with regard to the allegedly violated rights of the complainants—may not be irreversible in case CETA is incompatible with the German Constitution, a question the judges expressly left open to be decided in the main proceedings.

“The German Federal Constitutional Court issued a Solomonic, but somehow puzzling judgment on the request for temporary legal protection against the CETA.”

Regarding the first condition, the provisional application shall only concern those parts that undoubtedly fall within EU competence. The Court stressed that the German government itself declared not to agree to disputed areas and suggested that there may be problematic areas in certain chapters, including the dispute settlement system and portfolio investments (Chapters 8 and 13), maritime transport (Chapter 14), mutual recognition of professional qualifications (Chapter 11) and trade and labour (Chapter 23).

With regard to the second condition, the Court held that there appears to exist an imminent threat that any decision of the CETA committees could lead to conflicts with the identity of the German Constitution (“*Verfassungsidealität*,” Art. 79(3)). The Court thus required that any decision by a CETA committee may

only be taken after a common position taken by the Council as in Art. 218(9) of the Treaty on the Functioning of the European Union (TFEU) by unanimous vote, thereby supporting the “democratic backing” of these committees, but effectively granting a veto right to all EU member states on any decision to be taken in the respective committees.

“The Court suggested that Germany should remain in a position to terminate unilaterally the provisional application of CETA. It left open how this requirement could be achieved.”

On the last condition, the Court indicated that, should any of the dangers posed by CETA run risk to materialize, the German government should ensure the possibility to terminate the provisional application of CETA by a unilateral declaration. For that purpose, Germany should—in a way relevant in public international law—notify its understanding of its interpretation of CETA Art. 30.7(3)(c), namely, that Germany may unilaterally declare termination of CETA’s provisional application.

2. Some preliminary observations

The FCC has become notorious for its decisions on questions regarding the European Union, though less for the real outcome—in the end, it did not find Outright Monetary Transactions (OMT) to constitute an act *ultra vires* and neither did it try to stop CETA—than for its reasoning.

The Court has done three remarkable things. To begin with, it put the German government on a tight leash. Germany may only approve CETA under certain conditions that are not a mere nuisance, but require negotiating at EU level, maybe even with Canada. For that matter, CETA is categorized by the FCC as a “mixed agreement” requiring those regulations not within EU competence to be excluded from provisional application. It thereby entered into another dialogue with the Court of Justice of the European Union (CJEU), this time not on the protection of human rights or the power of the European Central Bank, but with regard to the delimitation of competence when it comes to the common commercial policy. It expressed its view as

to what the FCC finds to be fields of competence that might have remained within the sphere of competence of EU member states, especially with regard to investment protection. It is debatable whether one should go as far as to read this as a warning towards the CJEU not to go too far in the upcoming European Union–Singapore advisory opinion (Case A-2/15) by finding all aspects of trade and investment to fall into the explicit or implicit EU competence. However, it is beyond doubt that the Court could have been less explicit and avoid naming areas in order not to risk interfering with CJEU competence to interpret EU law.

Also with regard to CETA committees the FCC ventured deep into EU law. The Court interprets TFEU Art. 218(9) as requiring a unanimous Council decision with regard to CETA, given that, in the view of the FCC, these committees are “bodies” that would fall under said provision. However, these findings might constitute interpretations and suggestions overstepping the power of the German Court and would rather have to be clarified by the CJEU.

Finally, it brought public international law into play. The Court suggested that Germany should remain in a position to terminate unilaterally the provisional application of CETA. It left open how this requirement could be achieved.

CETA Art. 30.7(3)(c) provides: “A Party may terminate the provisional application of this Agreement by written notice to the other Party. Such termination shall take effect on the first day of the second month following that notification.”

If CETA is a mixed agreement, as suggested by the FCC, there will be 30 parties (at least as long as the United Kingdom remains in the European Union) covering competences of the European Union as well as of EU member states. However, the provisional application solely concerns “EU-only” parts. By its statement, the Court seems to suggest that Germany is a party to the agreement and is thus also in a position to terminate the provisional application “of this agreement” in the sense of CETA Art. 30.7(3)(c). Indeed, the term “a party” under CETA means Canada for the Canadian side, and the European Union as well as every EU member state for the European side.

However, if CETA is provisionally applied by a Council decision for the “EU-only” parts of CETA, Germany is bound via the general binding effect of EU law (TFEU Art. 216(2)). Can Germany by a unilateral act terminate the provisional application of “EU-only” parts of CETA? In my view a unilateral declaration of Germany cannot alter the binding effect of an agreement concluded by the European Union as this would alter a general provision of the TFEU. In that case,

any unilateral notification of termination by Germany would be entirely pointless, as it could not terminate the application of the “EU-only” parts of CETA.

Or could Germany act on behalf of the European Union? This could be based on the fact that, because a unanimous act is required in the Council, at any point in time any EU member state must be in a position to unilaterally terminate the provisional application. However, a unilateral declaration cannot be regarded as an act contrary to a unanimous decision of the European Council, and neither Germany nor any other EU member state can unilaterally act on behalf of the EU and its organs.

“A unilateral declaration cannot be regarded as an act contrary to a unanimous decision of the European Council, and neither Germany nor any other EU member state can unilaterally act on behalf of the EU and its organs.”

The third option is to argue more broadly with a view on the prospective entry into force of CETA. According to Article 25 of the Vienna Convention on the Law of Treaties between States and International Organizations or between International Organizations (VCLT-IO) a state or international organization is in a position to terminate the provisional application if it notifies the other parties of its intention not to become a party to the treaty. If CETA is a “mixed agreement,” ratification by all 30 parties is required in order for CETA to eventually enter into force. One could argue that a unilateral declaration by Germany based on the fact that CETA is not compatible with the German constitution would in effect mean that Germany will not ratify CETA. Under the principle of solidarity, the unilateral declaration could lead to a respective Council decision to notify Canada on the termination of the provisional application of CETA on behalf of the entire European Union side. This would however not reflect the unilateral power of termination as required by the FCC.

3. Conclusion: A Solomonic puzzle

What became again apparent is that the whole idea of

a “mixed agreement” is a nightmare for all involved—the European Union and its organs, EU member states, the European people and the courts that have to deal with the construction. In fact, negotiating an agreement as a single endeavour only to later divide and split it into parts and pieces might run counter to the spirit of any international agreement and does not pay enough attention to the fact that the parties agreed to the agreement as a single undertaking.

“Negotiating an agreement as a single endeavour only to later divide and split it into parts and pieces might run counter to the spirit of any international agreement.”

The Court was in a difficult position, less because difficult legal questions were posed to it—that is very much the task of a constitutional court to resolve—but because the judgment was issued in a request for temporary measures roughly 12 hours after the oral hearing took place. Any decision not cautious to the effects on all parties involved and affected could have detrimental consequences. Whether the Court, with its explicit naming of chapters when it comes to the question of competences, its strange requirement on the “democratic backing” of the committees and its rather puzzling condition regarding the ability to unilaterally terminate the provisional application of CETA, found a wise compromise rests with any observer of this ruling.* While observers still try to resolve the Solomonic puzzle posed by the FCC, the member states, EU and Canada signed CETA on October 30, 2016, and it will be provisionally applied after approval of the European Parliament. In the meantime, the complainants in this case again requested provisional measures based on the argument that the German government has not sufficiently fulfilled the conditions of the FCC.

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Notes

* Bundesverfassungsgericht. (2016, October 13), 2 BvR 1368/16. Applications for a Preliminary Injunction in the “CETA” Proceedings Unsuccessful. *Press Release No. 71/2016 of 13 October 2016*. Retrieved from <https://www.bundesverfassungsgericht.de/SharedDocs/Pressemitteilungen/EN/2016/bvg16-071.html>

India's Joint Interpretive Statement for BITs: An Attempt to Slay the Ghosts of the Past

Sarthak Malhotra



India has bilateral investment treaties (BITs) or bilateral investment promotion agreements (BIPAs) in force with 72 countries.¹ The initial duration of these agreements with 25 countries has not yet expired.² The Government of India (Government) has recently begun negotiations with these countries proposing a Joint Interpretive Statement (Statement)³ containing clarifications similar to the text of India's new Model BIT.⁴ We highlight below nine of the clarifications included in the Statement.

1. Definition of "investor"

According to the Statement (paragraph 2), the definition of "investor" includes only legal persons established under home state laws and having their seat in the home state. It also adds to the definition a requirement that the legal person be engaged in "substantial business operations," expressly excluding arrangements to avoid tax liabilities and the passive holding of assets such as stock, securities and land (paragraph 2.1(a)). In an attempt to promote the significance of "direct, real and transparent links" with the economies of the contracting states, the Statement affirms that the term "investor" shall not include domestic entities and those who invest through an entity of a non-contracting state (paragraph 2.2).

2. Definition of "investment"

Paragraph 4.1 clarifies that "investment" does not include pre-establishment activities. The Statement also lays down the test for determining what constitutes an "investment," based on the *Salini* test (paragraph 4.3).⁵ Learning from the unfavourable award in *White Industries v. India*,⁶ paragraph 4.3 excludes orders or judgments sought or entered in a judicial, administrative or arbitral action from the scope of "investment."

Finally, in a response to the many claims India is facing from large corporations like Vodafone and Cairn Energy related to its retrospective taxation demands, paragraph 5.1 clarifies that taxation measures are not protected by the BITs.

3. Fair and Equitable Treatment (FET)

The Statement clarifies that the country's obligation

under the FET standard only extends to the minimum standard of treatment under customary international law (paragraph 6.1). The Government's intention is to restrict the broad interpretation of the FET standard.⁷

It also provides under paragraph 6.2 that a breach of another provision of the BIT, or of a separate international agreement, shall not constitute a violation of FET, thus reaffirming that FET is an autonomous standard to be distinguished from others. In *Philip Morris v. Australia*, Philip Morris argued that Australia's alleged violations of obligations under certain World Trade Organization (WTO) agreements also constituted violations of the Australia–Hong Kong BIT through its umbrella clause. With this clarification in the Statement, the Government intends to shield itself against this type of argument.⁸

Under paragraph 6.3, measures taken for the protection or improvement of the following shall also not constitute breach of FET: (a) natural resources and the environment; (b) human, animal or plant life or health; (c) human capital, conditions of work and human rights; (d) economic conditions and the integrity of the financial system; and (e) implementation of fiscal policy measures, including taxation.

The Statement also clarifies that FET does not render contractual representations and promises enforceable under the BITs. Their legal significance has to be determined under the applicable law specified in the investment contract or under host state law (paragraph 6.5(a)).

4. "Effective Means" Obligation

In *White Industries*, even though the India–Australia BIT did not provide for an obligation to provide White Industries "effective means of asserting claims and enforcing rights,"⁹ the tribunal relied on the treaty's Most-Favoured-Nation (MFN) clause to borrow the "effective means" provision of the India–Kuwait BIT and hold India liable for judicial delay.

To avoid similar situations in future, the Statement clarifies that the "effective means" obligation is merely an obligation to not deny "access to legal or administrative adjudicatory proceedings in accordance with the procedure established by law" and does not create additional substantive obligations (paragraph 7.1). It also expressly states that normal delays in judicial or administrative proceedings do not violate the "effective means" requirement. Further, a breach of this provision shall only be established if the investor has exhausted all domestic remedies (paragraph 7.2).

5. Umbrella Clauses

The Statement clarifies that the specific contractual obligations brought under a BIT only include specific obligations entered in a written contract and do not include "acts by governmental, administrative or judicial authority solely in its regulatory capacity or an administrative or judicial consent decree or order" (paragraph 8.1). It also states that any interpretation

of such contractual obligations shall be in accordance with the applicable law specified in the contract (paragraph 8.2). However, to establish a violation of the umbrella clause, the investor would have to pursue the dispute resolution mechanism under the contract. Recourse to the BIT mechanism can only be had if no procedure is prescribed in the contract (paragraph 8.3). We believe that this may reduce the scope of the umbrella clause, as it reinforces the distinction between commercial arbitration and investment arbitration which umbrella clauses blur.

6. National Treatment (NT) and Most-Favoured-Nation (MFN)

The *White Industries* tribunal held that the MFN provision could be used to borrow substantive provisions—but not dispute resolution provisions—from third-party treaties. The Statement affirms that MFN does not allow cherry-picking of provisions of other treaties (paragraph 9.2(a)). It also reiterates the tribunal’s view that MFN does not apply to the dispute resolution mechanism contained in the BITs or to “other procedural and jurisdictional issues under any circumstance” (paragraph 9.2(b)).

The Statement also clarifies that the legitimate exercise of prosecutorial discretion, including discretion to enforce a law or regulation, shall also not amount to violation of MFN or NT, as long as the underlying law is not inconsistent with the BIT (paragraph 9.4).¹⁰

Under the Statement, the “like circumstances” test carried out in MFN and NT analyses must be “a fact-specific inquiry that is highly dependent on context.” For this purpose, the Statement offers guidance on relevant factors that must be considered, such as the actual and potential effects of the investments on the local community, and the aim of the policies or measures concerned (paragraph 9.3(b)).

7. Expropriation

The Statement affirms that determining whether a measure constitutes direct or indirect expropriation requires a case-by-case and fact-based inquiry. It also states that tribunals shall consider factors such as total or near-total and permanent destruction of the value of the investment and deprivation of rights of management and control over investment in determining whether an expropriation occurred (paragraph 10.2). Moreover, it clarifies that interference with management or control, when done in good faith and in compliance with host state laws such as financial or insolvency laws, would not constitute expropriation (paragraph 10.2(b)). Mirroring the newly added clarifications to the scope of FET, the Statement clarifies that measures taken for achieving certain public policy objectives shall not constitute expropriation (paragraph 10.3).

8. Essential Security Interests

To limit the scope of review by tribunals when the “essential security interests” defence is invoked, the Statement provides that, in such cases, it shall not be open to any tribunal to “review the merits of any such

decision, even where the arbitral proceedings concern an assessment of any claim for damages and/or compensation, or an adjudication of any other issues referred to the tribunal” (paragraph 11.1).

9. Dispute Settlement

To establish the existence of a dispute, an investor shall have to demonstrate that it has suffered actual and non-speculative damages as a direct and foreseeable result of the breach and that its claims are ripe for adjudication under the BIT (paragraph 12.1). As per paragraph 12.1(c), a claim will be “ripe” only if (a) it is based on a government conduct, (b) the government conduct is final and legally binding, and (c) the government conduct inflicts a definitive and concrete injury capable of being assessed as a breach.

Conclusion

The Statement seeks to find the right balance between protecting foreign investors and investments from certain types of government behaviour and maintaining states’ flexibility to adopt measures in the public interest. In particular, the clarifications on the FET and expropriation protections demonstrate India’s commitment to ensure that its right to regulate is not impeded. The Statement also seeks to mold BITs into a tool to promote ethical business practices. It raises important points to be addressed in reforming India’s foreign investment regime, and could encourage other developing countries to undertake similar reforms.

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Notes

1 United Nations Conference on Trade and Development (UNCTAD). (2016). *International investment agreements navigator (IIA navigator)*. Retrieved from <http://investmentpolicyhub.unctad.org/IIA/CountryBits/96#iialnnerMenu>.

2 These countries are Bahrain, Bangladesh, Bosnia and Herzegovina, Brunei, China, Colombia, Finland, Iceland, Jordan, Kuwait, Laos, Latvia, Libya, Lithuania, Macedonia, Mexico, Mozambique, Myanmar, Saudi Arabia, Senegal, Serbia, Sudan, Syria, Trinidad and Tobago, and Turkey.

3 India’s Consolidated Interpretive Statement. (2016, February 8). Retrieved from http://indianbusiness.nic.in/newdesign/upload/Consolidated_Interpretive-Statement.pdf.

4 Government of India. (2015). *Model text for the Indian bilateral investment treaty*. Retrieved from http://indianbusiness.nic.in/newdesign/upload/Model_BIT.pdf.

5 For a detailed discussion, see Grabowski, A. (2014). The definition of investment under the ICSID Convention: A defense of Salini. *Chicago Journal of International Law*, 15(1), 287–309. Retrieved from <http://chicagounbound.uchicago.edu/cjil/vol15/iss1/13>.

6 *White Industries v. India*, Final Award, November 30, 2011. Retrieved from <http://www.italaw.com/sites/default/files/case-documents/ita0906.pdf>.

7 We believe that the actual effect may not necessarily be so, since, according to the interpretation of several arbitral tribunals, the minimum standard of protection under customary international law has evolved due to the impact of BITs on protection of alien property. See, for example, *Chemtura v. Canada*, Final Award, October 2, 2010, para. 121. Retrieved from http://www.italaw.com/sites/default/files/case-documents/ita0149_0.pdf; *Mondev v. United States*, ICSID Case No. ARB(AF)/99/2, Award, October 11, 2002, paras. 116–117. Retrieved from <http://www.italaw.com/sites/default/files/case-documents/ita1076.pdf>.

8 See *S.D. Myers v. Canada*, First Partial Award, November 13, 2000. Retrieved from <http://www.italaw.com/documents/SDMyers-1stPartialAward.pdf>.

9 *White Industries*, *supra* note 6, paras. 11.4.19–20.

10 In *Apotex v. United States*, the tribunal held that the U.S. Federal Drug Administration (FDA)’s decision to impose an “Import Alert” on certain drugs manufactured by Apotex but not on other drug manufacturers with comparable problems amounted to de facto discrimination. However, the tribunal ultimately found the discrimination to be for a legitimate purpose and therefore justified under the North American Free Trade Agreement (NAFTA). *Apotex v. United States of America*, ICSID Case No. ARB(AF)/12/1, Award, August 25, 2014. Retrieved from <http://www.italaw.com/sites/default/files/case-documents/italaw3324.pdf>.

Special and Differential Treatment in International Investment Agreements

Riham Marii



1. Origins of S&D treatment

Special and Differential Treatment (S&D)—originally forged in the Multilateral Trading System (MTS) in the 1960s to provide greater flexibility for developing countries in trade commitments—has significantly evolved in trade negotiations and also gained momentum in investment agreements.

Historically, S&D in the trade context emerged from the call for differentiation concerning the extent, exemptions and assistance afforded to developing countries. S&D was codified as a normative rule of the General Agreement on Tariffs and Trade (GATT) in 1979 in the so-called “enabling clause,” which provides for preferential treatment for developing countries, on a non-reciprocity basis, in a manner commensurate with their development needs. It provides greater policy space for developing countries,¹ reflecting the fundamental idea that “no one size fits all.” The decision embedded in the GATT allowed developing countries to deviate from most-favoured-nation (MFN) clauses and other non-discrimination obligations, establishing a Generalized System of Preference (GSP) in the MTS. Essentially, the pre-Uruguay GSP provided for preferential rights for developing countries, including enhanced market access, flexibility in adopting protective measures and reservations, and a waiver of some of the GATT disciplines.²

By rebalancing the international law principle of sovereign equality, which calls all states—irrespective of their level of development—to equally abide by international agreements, S&D aims to enable developing countries to abide by their commitments without hindering their development process. The concept has gained prominence following the entangled debate on the relationship between trade and development. It has also built on the economic inequalities that justify the application of the differentiation principle to developing countries, stipulating that “market access would need to be established on terms that benefit the least advantaged.”³ In this context, S&D treatment emerged to formally accord developing countries some flexibilities and preferences to implement economic agreements, depending on their needs and capabilities.

2. S&D: From trade to investment

For the same reasons, S&D was later mirrored in

international investment agreements, mainly in those between developing countries. In particular, South–South regional agreements encapsulated annexes of reservations, allowing each contracting party to take into account its national policy objectives.

Arguably, S&D was triggered on the basis of the 1969 Vienna convention on the 1969 Vienna Convention on the Law of Treaties, which defines reservation as “a declaration made by a State by which it purports to exclude or to alter the legal effect of certain provisions of a treaty in their application to that State.”⁴ In this context, international law forges discretionary margins to determine the extent of each reservation. In a more general sense, reservations are regarded as a tool to adjust treaty obligations to comply with state laws and regulations.

Preferential rights for developing countries gained momentum in the 1980’s with the growing perception of market externalities and spillovers on domestic industries and enterprises of host states. This is especially true for developing countries, since their domestic enterprises may be particularly vulnerable, especially vis-à-vis large multinational investors. Therefore, some developing countries incorporated these imperatives in their early agreements. See, for example, the 1988 China–Japan bilateral investment treaty (BIT): “it shall not be deemed ‘treatment less favorable’ for either Contracting Party to accord discriminatory treatment, in accordance with its applicable laws and regulations, to nationals and companies of the other Contracting Party, in case it is really necessary for the reason of public order, national security or sound development of national economy.”⁵

This then-unprecedented approach started to become prominent in regional agreements. The 1980 Unified Agreement for the Investment of Arab Capital in Arab States explicitly allows states to accord preferential privileges to some investors or projects that aim at fostering the development of the national economy, regional integration and transfer of technology.⁶ Also notably, the 1987 Agreement for the Promotion and Protection of Investments of the Association of Southeast Asian Nation (ASEAN), in addition to countries’ specific reservations prescribed in annexes, contains a general provision requiring that investments be aligned with national policy objectives, national laws and regulations.⁷

Additionally, a wider notion of S&D was included in the 2006 Protocol on Finance and Investment of the Southern African Development Community (SADC). It provides for carve-outs allowing preferential treatment for some investments and investors in order to achieve national development objectives. It also provides for more favourable conditions for least developed countries (LDCs) based on non-reciprocity and mutual benefits, and ensures preferential treatment for LDCs with respect to markets openings and derogations of incentives.⁸ S&D also was reflected in assistance LDCs received out of this regional cooperation aimed at boosting member states’ development through investment.

Recent regional agreements include explicit clauses on S&D treatment to carve out some investments or economic activities from the treaty or some of its provisions. They also provide for temporary suspensions and gradual application of the treaty or certain provisions—a transition period

to grant flexibility for states to address developmental needs and other economic concerns faced in reducing the operational disparities of these agreements. For example, the 2015 draft Pan African Investment Code (PAIC), in addition to reservation schedules and measures carved out of national treatment and MFN, provides for development-oriented performance requirements; preferential treatment to qualifying investments and investors, commensurate with national development objectives; and interim periods.⁹

3. Resurgence of S&D in BITs: An intriguing context

While S&D appears explicitly in South–South regional agreements, prescribing a minimum level-playing field between the parties while providing leeway to implement their national policy objectives, historically it only appeared indirectly in BITs, not in stand-alone clauses, but within the context of FET, national treatment and other provisions. However, S&D treatment has gained prominence in recent model BITs with explicit language allowing for a modulation of commitments and providing support, beyond those providing substantial and concrete preferences as prescribed in the countries' reservation schedules. New features of S&D include safeguard measures, performance requirements, obligations regarding transfer of technology and other measures of support, general carve-outs, and other procedural flexibilities implying a reduced level of commitment depending on the state's level of development.

Recent model BITs illustrate a growing pattern of modulation for existing commitments. For instance, Egypt's updated BIT model reflects the country's interest in promoting sustainable development while considering the country's development level, as considerably reflected in the newly modulated national treatment and MFN clauses. It also invokes international law instead of setting a stand-alone standard in this regard, especially with respect to fair and equitable treatment (FET) and physical security protection.

The Indian Model BIT omits MFN and FET clauses altogether, and carves out government procurement measures from the scope of the treaty, implicitly affording preferential treatment to domestic investors.¹⁰ Additionally, it allows flexibility for states to adopt certain measures on the basis of legitimate public interests such as environment, public health, safety, and public order, without engaging state liability for breach of the treaty. These measures must be taken on a non-discriminatory and non-arbitrary basis, in good faith and in like circumstances.¹¹

Similarly, Brazil's Agreements on Cooperation and Facilitation of Investments (ACFIs) provide for MFN and national treatment subject to legitimate public welfare objectives. The ACFIs devote a special focus to investment facilitation through promoting technological, scientific and cultural cooperation. The agreements provide for exchange of information, expertise and transfer of technology, and allow for development measures without jeopardizing the states' security concerns.¹² These new features reflect the causality between investment and development, and are designed to align investment with national policy objectives for development.

Differently from the trade context, S&D in investment treaties tends to derogate treatment on a non-discriminatory basis by triggering more favourable treatment in line with the country's level of development. However, investment treaties are similar to trade law in

that they adopt an approach based on excluding some obligations from the scope of the agreement, giving the state the right to derogate from certain commitments which may impair its sovereignty or which do not streamline its legitimate development interests.

4. Conclusion

Theoretically justified in the MTS to allow states to have differentiated responsibilities under the same agreement, S&D treatment arose in the investment regime to offset the imbalances of North–South treaties, naturally reflecting the increased momentum of sustainable development concerns. South–South regional investment agreements triggered S&D treatment widely to promote investment between signatories. This resonated with developing countries, which advocated in the MTS at that time for a more favourable and efficient operation of trade agreements intended to promote development.

Although South–South regional investment agreements provided for the required balance of the investment regime, the imbalance in North–South investment agreements remained undeniable. Consequently, it is uncertain whether S&D treatment will continue to be explicitly included in developing country BIT models and North–South BITs, as they deviate in major ways from the positions of developed countries.

Lastly, it is important to remember that S&D treatment depends on how states tailor and adjust their obligations in a manner conducive to their development, according to their national policy interests. However, the resurgence of a broader and explicit S&D treatment, although timely in the context of reform of the investment regime, leaves some thoughts on rethinking how S&D will be perceived in the new investment context.

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UNCTAD's International Investment Agreements Conference 2016: Taking IIA Reform to the Next Level

James Zhan and Diana Rosert



As part of the World Investment Forum (WIF) 2016,¹ negotiators of international investment agreements (IIAs) and various stakeholders convened at the High-Level IIA Conference on July 19, 2016 in Nairobi, Kenya. Some 50 country delegates, parliamentarians, officials of international organizations and civil society representatives discussed the first phase of IIA reform and how to move to the next phase.

The “first phase” refers to IIA reform processes that started a few years ago and are now the new normal in international investment policy-making: many countries reviewed their IIA networks, developed model treaties with refined provisions and negotiated more sustainable-development-friendly treaties; others have started such processes. According to the **World Investment Report 2016**, over 100 countries have engaged in IIA reform, often using the **Investment Policy Framework for Sustainable Development** and the **Roadmap for IIA Reform** prepared by the United Nations Conference on Trade and Development (UNCTAD) as guidance. Building on the lessons learned so far, “phase two” aims at comprehensive reform, also addressing the stock of IIAs.

While the degree of IIA reform engagement and the approaches taken continue to vary across countries and regions, a consensus on the need for IIA reform emerged in the first phase. The speakers at the IIA Conference unequivocally supported IIA reform, and a common message was that it should promote sustainable development objectives, safeguard the right to regulate and pursue a balanced approach, while protecting and promoting foreign investment.² Another recurring message was the need for a more coordinated approach to the reform of investment treaties and dispute settlement, including through intensified dialogue at the multilateral level. Several speakers considered that phase two should address the fragmented nature of current reform responses.

The IIA Conference was marked by a great willingness to consider options and new suggestions for the

next phase of IIA reform. Several speakers saw opportunities for collaboration in the long term, for example with regard to a multilateral investment court, an appellate mechanism or guiding principles for investment policy-making. At the same time, a note of caution was perceptible concerning certain novel approaches to investment dispute settlement.

G20 Guiding Principles for Global Investment Policy-Making

Representatives of individual G20 members speaking at the IIA Conference welcomed the G20 Guiding Principles for Global Investment Policy-Making and acknowledged UNCTAD's contribution to their elaboration. The **non-binding Guiding Principles** were agreed on during the **G20 Ministerial Meeting** in Shanghai in July and endorsed by G20 leaders at the Hangzhou Summit in September. A few statements alluded to the development of South–South Principles on International Investment for Sustainable Development, which was the topic of a **side event** organized by the International Institute for Sustainable Development (IISD) and the Kenya Investment Authority (KenInvest) during the WIF. The side event discussed the need and feasibility of developing principles to enhance South–South cooperation for comprehensive reform of the investment regime.

Investment facilitation in IIAs and beyond

Many speakers considered that investment facilitation was among the most pressing issues on the reform agenda for phase two, also drawing on UNCTAD's Global Action Menu for Investment Facilitation.³ In light of the trillion-dollar financing gap for the sustainable development goals (SDGs), they suggested that facilitation measures should come into focus as a tool to mobilize investment for sustainable development, particularly into infrastructure development.

“A common message was that IIA reform should promote sustainable development objectives, safeguard the right to regulate and pursue a balanced approach, while protecting and promoting foreign investment.”

The participants observed that investment facilitation provisions were largely absent from IIAs. Noting that UNCTAD's Action Menu included actions to strengthen investment facilitation aspects in IIAs, several speakers supported the inclusion of such provisions. One delegate added that the country used a new model that incorporated investment facilitation provisions and reflected the elements proposed in the UNCTAD Action Menu.

The role of investment facilitation measures at the national level and related institutions—such as investment promotion agencies, one-stop shops and inter-ministerial committees—was also stressed. Several participants suggested that, building on UNCTAD's Action Menu, facilitating investment through national and international policies should be explored further.

Right to regulate and responsible investment

Many speakers considered that preserving the right to regulate and balancing the rights and obligations of states and investors were principal IIA reform objectives. Several speakers also suggested that IIAs should address the promotion of human rights and the protection of health, environmental and labour standards. Some noted that their IIAs included language to this effect. The Canada–European Union Comprehensive Economic and Trade Agreement (CETA), which contains an article reaffirming the right to regulate and a “non-stabilization” clause, was mentioned as a recent treaty example. Several speakers expressed their commitment to promote responsible investment. One stakeholder suggested that UNCTAD and other organizations need to work more on enforceable investor obligations in IIAs and on the nexus between investment and sustainability.

With regard to the substantive content of IIAs, the participants identified the definitions of investment and investor, fair and equitable treatment, indirect expropriation, the umbrella clause, denial of benefits and the survival clause as provisions to be addressed in reform efforts. Among others, further research was suggested on the definition of portfolio investment, the term “substantial business activities” and the scope of the right to regulate.

Reform of investor–state arbitration: court systems, appellate mechanisms and alternative dispute resolution

Further exploring options to reform investor–state arbitration was seen as an ongoing task for the next reform phase. Many speakers welcomed the EU proposal for an investment court system, consisting of a first instance tribunal and an appellate tribunal, and its incorporation into EU agreements with Canada and Viet Nam. It was seen as an innovative option to address legitimacy and other concerns related

to the existing investor–state dispute settlement (ISDS) mechanism. EU member states and a few non-EU countries stressed the need for an appellate mechanism to increase consistency in ISDS decisions.

The EU representative and several EU member states suggested that including investment court systems in individual treaties could be a step toward creating a multilateral investment court. One participant added that a multilateral treaty could create such a court to replace arbitral tribunals under current treaties. Another speaker cautioned that it was uncertain whether an investment court would deliver increased fairness and impartiality and that this approach might carry risks.

Several speakers suggested strengthening dispute prevention and alternative dispute resolution mechanisms. Some representatives outlined the steps their countries were taking in domestic laws and investment treaties to encourage the settlement of disputes by means other than arbitration. For example, they created joint committees entrusted with the mediation of disputes or ombudspersons to facilitate investor–government relationships.

Some speakers also suggested exploring domestic and regional courts as alternatives to arbitration. One speaker referred to the country's new model treaty, which requires the exhaustion of local remedies before recourse to arbitration. Another country representative presented a treaty approach that relied on state–state arbitration rather than ISDS. Two other speakers noted that ISDS was a necessary component of IIAs.

To assist countries with limited resources and expertise, one country representative proposed a legal advisory agency on investment dispute settlement, for example modelled after the Advisory Centre on World Trade Organization (WTO) Law.

“Many speakers considered that preserving the right to regulate and balancing the rights and obligations of states and investors were principal IIA reform objectives. Several suggested that IIAs should address the promotion of human rights and the protection of health, environmental and labour standards.”

Intensified collaboration and coordination for phase two of IIA reform

Several speakers discussed how to address the challenge of increasing fragmentation in IIA reform efforts and treaty-making. Some suggested that more dialogues and exchanges were desirable at the multilateral level. As potential avenues for such multilateral engagement, speakers identified discussions on setting-up a multilateral investment court or a global appellate mechanism and consensus-building on the scope of key provisions. The latter could be supported by the sharing of best practices.

Consensus-building, intensified collaboration and coordination among countries could also help deal with the deficiencies in existing treaties. More specifically, one speaker suggested exploring whether the UN Convention on Transparency in Treaty-based Investor-State Arbitration (Mauritius Convention) could serve as a model for a mechanism to reform the large stock of investment treaties that do not contain the safeguards and clarified language of more recent treaties.

“Some speakers suggested that more dialogues and exchanges were desirable at the multilateral level. Consensus-building, intensified collaboration and coordination among countries could also help deal with the deficiencies in existing treaties.”

Several speakers emphasized their openness to learn from other approaches and suggested that flexibility, pragmatism, openness and creativity could facilitate IIA reform. One participant stressed the role of civil society in reform efforts.

Many speakers called for an increase in capacity-building and technical assistance activities by UNCTAD and others to support efforts to reform complex IIA networks, particularly in developing and least developed countries. Several developing country speakers drew attention to the challenges in treaty negotiations and renegotiations. It was noted that the UNCTAD Investment Policy Framework and Roadmap for IIA Reform provided useful guidance in this regard. UNCTAD was asked to develop more policy tools to support IIA reform processes, for example through a

checklist or action plan for phase two of reform.

Many speakers asked UNCTAD and other organizations such as the Organisation for Economic Co-operation and Development (OECD) and the United Nations Commission on International Trade Law (UNCITRAL) to continue to provide platforms for policy dialogue on IIA and ISDS reform.

Renewed mandate on IIAs and sustainable development

In parallel with the WIF, the 194 UNCTAD member states met in Nairobi for the 14th session of UNCTAD and reached consensus on UNCTAD's work program for the next four years. The outcome document—the **Nairobi Maafikiano**—gives a central role to UNCTAD in delivering the SDGs and covers a broad range of activities in the trade, investment and development area. It also states that UNCTAD should “continue its existing programme of meetings and consultations with member States on [IIAs] in accordance with the Addis Ababa Action Agenda, maintaining its role as a forum for international discussion on [IIAs], and assist member States in their efforts to strengthen the development dimension, as appropriate” (paragraph 38(l)). UNCTAD should also continue to “promote a better understanding of issues related to [IIAs] and their development dimension” (paragraph 55(hh)). This provides a solid framework for UNCTAD's work on IIA reform in the years to come.

Video recordings and statements of the IIA Conference are available at <http://unctad-worldinvestmentforum.org/programme2016/international-investment-agreements-conference-2016>.

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The views expressed in this article are those of the authors and do not necessarily reflect the views of UNCTAD.

Notes

¹ UNCTAD's WIF is a high-level, biennial, multi-stakeholder gathering designed to facilitate dialogue and action on the world's key emerging investment-related challenges. See <http://unctad-worldinvestmentforum.org>.

² UNCTAD's Investment Policy Framework on Sustainable Development was used as a reference.

³ UNCTAD's Global Action Menu for Investment Facilitation was at the centre of the debate throughout the WIF 2016. A number of individual events referred to the need to bolster investment facilitation through a concrete global action plan. The September 2016 update of UNCTAD's Global Action Menu is available at <http://investmentpolicyhub.unctad.org/News/Hub/Home/519>.

news in brief

Trump election affects mega-regional negotiations including TTIP, TPP and RCEP

In September, **EU officials recognized** that the negotiations on the EU–U.S. Transatlantic Trade and Investment Partnership (TTIP) were unlikely to be concluded before the end of U.S. President Barack Obama’s mandate. After November 9, when protectionist Republican candidate Donald Trump won the U.S. presidential elections, the future of TTIP negotiations became even less clear. EU Trade Commissioner Cecilia Malmström said on November 11: **“TTIP will probably be in the freezer** for quite some time and then what will happen when it is defrosted, I think we will need to wait and see.”

While Trump’s position on TTIP may be unclear, he strongly campaigned against existing multilateral trade deals, including the Trans-Pacific Partnership (TPP) **signed earlier this year** and even the North American Free Trade Agreement (NAFTA), in force since 1994. On November 22, **the President-elect announced** that among his actions on his first day in office (January 20, 2017) would be the full withdrawal of the United States from the TPP, characterizing it as “a potential disaster” for the country. “Instead, we will negotiate fair, bilateral trade deals that bring jobs and industry back onto American shores,” he added.

In response, **Japanese Prime Minister Shinzo Abe stated** that “the TPP would be meaningless without the United States.” The TPP—concluded by Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States, and Vietnam—includes a clause preventing entry into force without U.S. ratification. **Peruvian Trade Minister Eduardo Ferreyros proposed** new talks: “We can modify that clause and also take advantage to modify other clauses that might be uncomfortable for us.” **Australian Trade Minister Steven Ciobo also said** that countries could push ahead by amending the agreement and possibly adding new members.

Analysts see in the U.S. withdrawal from the TPP an opportunity for China to assume leadership in Asia-Pacific trade and investment negotiations. China is negotiating the Free Trade Area of the Asia Pacific (FTAAP) and the Regional Comprehensive Economic Partnership (RCEP). The latter excludes the United States, but includes Australia, India, Japan, New Zealand and South Korea, as well as the ten member states of the Association of Southeast Asian Nations (ASEAN). During the Asia-Pacific Economic Cooperation (APEC) summit in Peru on November 19 and 20, **Tan Jian, a senior Chinese delegate, said** that Chile, Peru and other countries now intend to join RCEP negotiations, and that current negotiating partners aim at concluding the deal as soon as possible to counter protectionism.

Brazil and India initial bilateral investment treaty (BIT); text yet to be published

During the **10th Annual Forum of Developing Country Investment Negotiators**, held in Colombo, Sri Lanka, from November 7 to 10, representatives from Brazil and India announced that they had recently initialled a bilateral investment agreement (BIT).

Since 2015, Brazil has concluded seven BITs (with Angola,

Chile, Colombia, Malawi, Mexico, Mozambique and Peru) based on its **new model Agreement on Cooperation and Facilitation of Investments (ACFI)**, which focuses on investment facilitation and dispute prevention through the creation of ombudsmen in each contracting state and a joint committee. In December 2015, India approved a revised **model BIT**, which—while including a provision on the standard of treatment—avoids the term “fair and equitable treatment” (FET) and the most-favoured-nation (MFN) treatment clause, and includes investor obligations.

It is reported that the Brazil–India BIT incorporates elements from both approaches. For example, in line with Brazil’s approach, it includes elements of investment cooperation and facilitation, and focuses on dispute prevention rather than providing for investor–state arbitration; in line with the Indian model, it does not refer to FET and does not include an MFN clause.

CETA signed; Canada and European Union to “work expeditiously” on creating a Multilateral Investment Court

On October 30, during the 16th European Union–Canada Summit held in Brussels, the two negotiating partners signed the **Comprehensive Economic and Trade Agreement (CETA)**, after seven years of negotiations. European Commission **President Jean-Claude Juncker hailed it** as “the best trade agreement the European Commission has ever negotiated” and added that it will set global standards for other trade agreements.

Canadian and EU leaders have also signed a **Joint Interpretative Instrument** in which they recognize “the right to regulate in the public interest” as a fundamental value. The instrument characterizes CETA as “an important and radical change in investment rules and dispute resolution” and as the basis for a Multilateral Investment Court, which Canada and the European Union have committed to “work expeditiously” to create.

The signing of the agreement had been thrown into doubt just a few weeks before. On October 18, the sub-national parliament of the Belgian region of **Wallonia voted** not to give powers to the Belgian federal government to sign CETA. The signing ceremony that had been scheduled for October 27 was cancelled as a result. On the same day, Belgian political leaders reached an **agreement to support CETA**.

In the **agreement**, Wallonia is reported to have obtained assurances that CETA would not harm local farmers, that states’ participation in the **Investment Court System (ICS)** mechanism would depend on specific approval by individual EU member states, and that Belgium would ask the Court of Justice of the European Union (CJEU) for an advisory opinion on the compatibility of the ICS mechanism with EU law.

Ratification by the European Parliament **will be required** for CETA to apply provisionally to the European Union. However, reportedly due to the Wallonia deal, ICS will be left out of the scope of provisional application. Accordingly, ICS will only be implemented after ratification by individual EU member states. In the meantime, Canadian and EU officials will elaborate on the details of the system, including the selection of judges, access to ICS by smaller businesses and the appellate mechanism.

awards and decisions

Venezuela to pay US\$1 billion for expropriating Canadian mining company's investment

Rusoro Mining Ltd. v. the Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/12/5

Claudia María Arietti López

In an award dated August 22, 2016, a tribunal at the Additional Facility (AF) of the International Centre for Settlement of Investment Disputes (ICSID) ordered Venezuela to pay US\$966.5 million plus interest to Canadian company Rusoro Mining Limited (Rusoro) for unlawfully expropriating its mining investment.

Background and claims

Between 2006 and 2008, through the acquisition of controlling interests in 24 Venezuelan companies, Rusoro indirectly acquired 58 mining concessions and contracts to explore and produce gold in Venezuela.

At that time, Venezuela had already established, among other restrictions, a limitation in the exportation of gold. In April 2009, it introduced further limitations, and in July 2010 it relaxed the rules for public companies while reaffirming the limitations for private companies. Finally, in July 2010, Venezuela reduced the restrictions and unified the regime for public and private producers.

On August 17, 2011, then-President Hugo Chávez announced the nationalization of the gold mining industry in Venezuela. On September 16, 2011, he issued a nationalization decree that provided for state control of the property and mining rights of all gold producing companies and ordered the transfer of all existing concessions or contracts to mixed companies controlled by the state.

After six-month negotiations, Rusoro and Venezuela could not reach an agreement on the compensation amount. Consequently, on July 17, 2012, Rusoro initiated arbitration proceedings, claiming that Venezuela expropriated its investment, among other breaches of the Venezuela–Canada bilateral investment treaty (BIT). Rusoro asked for a compensation of roughly US\$2.3 billion plus interest.

Tribunal dismissed all of Venezuela's jurisdictional objections

First, Venezuela argued that since Rusoro's expropriation claims were also based on measures taken by Venezuela in 2009 and 2010, the dispute was time-barred by the three-year statute of limitation contained in the BIT. The tribunal determined that only measures taken by Venezuela before July 17, 2009 (three years before the filing of the request for arbitration) were time-barred.

In its second objection, Venezuela argued that there was no jurisdiction before the ICSID AF, since it had already withdrawn from the ICSID Convention when the arbitration was registered (in August 2012). The tribunal, agreeing with Rusoro, and in line with the decision in the *Venoklim v. Venezuela* case, held that the relevant

date was the date of the request (July 17, 2012), when Venezuela was still an ICSID member state.

Venezuela also stated that Rusoro breached Article 29 of Venezuela's mining law, which requires prior authorization from the Ministry of Mines before acquiring mining rights, and therefore, it was not a protected investor and did not have a protected investment under the BIT. The tribunal disagreed with Venezuela and concluded that Article 29 of the mining law does not apply to the indirect acquisition of companies that hold mining rights.

Rusoro's direct expropriation claims upheld as Venezuela failed to ensure "prompt, adequate and effective compensation"

Rusoro argued that, through the 2011 nationalization decree, Venezuela expropriated its investment in violation of the BIT. In turn, Venezuela indicated that the BIT contemplated nationalization and that it complied with the BIT's requirements, except for compensation. According to Venezuela, the failure to agree on the amount of compensation does not render nationalization unlawful *per se*.

Since both parties coincided that an expropriation took place, the tribunal then analyzed the lawfulness of the expropriation. It noted that while Venezuela's expropriation was adopted for a public purpose, under due process of law and in a non-discriminatory manner, it failed to ensure prompt, adequate and effective compensation to Rusoro. Accordingly, it found that the expropriation was unlawful.

Regarding the public purpose requirement, the tribunal pointed that states have discretion in establishing their public policy and that the nationalization decree clearly stated the public purpose of the expropriation.

In addition, the tribunal held that the expropriation was carried out under due process of law because Rusoro had two options under Venezuelan law to challenge the nationalization decree, but never pursued them.

Concerning the non-discrimination prerequisite, the tribunal found that both Venezuelan and foreign investors were equally affected by the nationalization decree.

Regarding the compensation requirement, Rusoro alleged that it never received any compensation and that the negotiation was a "mere window dressing" (para. 398), since the nationalization decree limited compensation to book value. Venezuela, conversely, stated that it negotiated with Rusoro in good faith for six months and that Rusoro remained uncompensated because it rejected Venezuela's offer.

The tribunal pointed out that the standard for compensation established in the BIT was the "genuine value" of the investment, which should be deemed to be the same as "fair market value." It also indicated that the nationalization decree established a different standard, namely, the book value of the investment.

The tribunal finally referred to the fact that Venezuela neither paid the amount offered nor deposited it in escrow in favor of Rusoro.

Alternative claim of creeping or indirect expropriation deemed unconvincing

Rusoro also claimed that it suffered indirect expropriation as result of a series of measures taken by Venezuela starting in 2009 that culminated with the nationalization decree. The tribunal dismissed this claim as it did not find convincing evidence that, before enacting the nationalization decree, Venezuela had envisioned and implemented a plan to nationalize the gold sector.

Success of ancillary claim that Venezuela's increased restrictions on gold exports breached the BIT

Rusoro submitted several ancillary claims. The tribunal concluded that it failed to prove that Venezuela breached the BIT provisions regarding fair and equitable treatment, full protection and security, non-discrimination and free transfers. However, it found that Venezuela breached the BIT by imposing an increased restriction on the exportation of gold.

Rusoro claimed that, with the 2010 measures, Venezuela imposed various restrictions on Rusoro's ability to export gold in breach of the BIT's prohibition on export restrictions. The tribunal agreed. It noted that, while at the time Rusoro made its investment, the regulations in force allowed 85 per cent of the production to be exported, the 2010 regulation reduced that figure to 50 per cent.

Tribunal used average of three methodologies to calculate compensation

To find the "adequate compensation" amount to be paid by Venezuela to Rusoro for unlawful expropriation, the tribunal first noted that there were two issues on which the parties agreed: the proper valuation date was the date of the nationalization decree, and the "genuine value" of the investment was the "fair market value."

In assessing the fair market value of the investment, the tribunal found that the best method to determine the quantum was to combine three methods of valuation: it gave 25 per cent weight to the maximum market valuation (US\$700.6 million), 25 per cent to book valuation (US\$908 million) and 50 per cent to the adjusted investment valuation (US\$1.1 billion). Based on the above, the tribunal determined that the valuation of the investment on September 16, 2011 was \$966.5 million.

The tribunal also ordered Venezuela to pay US\$1.2 million as damage for breaching the BIT in connection with export limitations, and awarded pre- and post-award interest on the total amount of the award at the rate of USD LIBOR for one-year deposits, plus 4 per cent, compounded annually.

Notes: The ICSID AF tribunal was composed of Juan Fernandez-Arnesto (President, appointed by the

parties, Spanish national), Francisco Orrego Vicuña (claimant's appointee, Chilean national) and Bruno Simma (respondent's appointee, German national). The award is available at: <http://www.italaw.com/sites/default/files/case-documents/italaw7507.pdf>.

ICSID tribunal dismisses MFN clause in WTO GATS as a means of importing Senegal's consent to arbitration from third party BIT

Menzies Middle East and Africa S.A. and Aviation Handling Services International Ltd. v. Republic of Senegal, ICSID Case No. ARB/15/21

Suzy H. Nikièma

In an award rendered on August 5, 2016, an International Centre for Settlement of Investment Disputes (ICSID) tribunal declined jurisdiction to hear an application for arbitration against Senegal. In particular, the tribunal accepted Senegal's objection to jurisdiction, while rejecting the invocation of the most-favoured-nation (MFN) clause in the General Agreement on Trade in Services (GATS) of the World Trade Organization (WTO) to import consent by Senegal to international arbitration.

Background and claims

The claim was filed on April 17, 2015 by Menzies Middle East and Africa S.A. (Menzies), a company registered in Luxembourg, and Aviation Handling Services International Limited (AHSI), a company registered in the British Virgin Islands.

In November 2003 the claimants acquired AHS SA, a company under Senegalese law created for the conduct of ground handling activities at airports in Senegal.

According to the claimants, Mamadou Pouye and the brothers Ibrahim and Karim Aboukhalil, were the economic beneficiaries of the two companies that controlled AHS SA. Senegal argued instead that the economic beneficiary was in fact Karim Wade, son of the former President of Senegal and former Senegalese Minister of Air Transport.

AHS SA carried out its activities until 2013, when the Court for the Suppression of Illicit Enrichment (CREI, in its French acronym) opened an investigation against Wade, Pouye and the Aboukhalil brothers for illicit enrichment and collusion in illicit enrichment. As part of these proceedings, AHS SA was placed by CREI under temporary administration as a precautionary measure.

In March 2015 Wade was found guilty of illicit enrichment, and Pouye and the Aboukhalil brothers were found guilty of collusion in illicit enrichment. On order of CREI, their assets were confiscated, including their shares in AHS SA. The decision was confirmed by the Supreme Court of Senegal in August 2015.

In their claim to the ICSID tribunal, the claimants alleged that the placement of AHS SA under administration and the disastrous management that followed were not only illegal under Senegalese law, in particular the investment code, but also constituted

indirect expropriation and a discriminatory measure under general international law and Senegal's bilateral investment treaties (BITs) with the Netherlands and with the United Kingdom. They also alleged that the decision of the Supreme Court was arbitrary. Menzies and AHSI demanded total damages of €41,633,169.

Senegal, in rejecting the allegations, raised three objections to jurisdiction: absence of consent to arbitration (lack of jurisdiction *ratione voluntatis*); the non-existence of an investment made in Senegal (lack of jurisdiction *ratione materiae*); and the Senegalese nationality of the claimants (lack of jurisdiction *ratione personae*).

Analysis of jurisdiction ratione voluntatis by the tribunal

The question raised by the first objection was whether the state had given its consent to arbitration. To do this, the arbitrators considered the rules invoked:

(a) Article II(1) of the GATS, which provides that “each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country” (from the English version of the GATS).

(b) Article 12.2 of the investment code of Senegal, which provides that “disputes between a foreign natural or legal person and the Republic of Senegal [...] shall be settled in accordance with the arbitration procedure [...] arising [...] from agreements and treaties on the protection of investments made between the Republic of Senegal and the State of which the investor is a national.”

(c) The dispute settlement provisions contained in the Senegal–Netherlands BIT (article 10) and the Senegal–United Kingdom BIT (article 8).

The tribunal firstly considered the case of Menzies (A), before addressing that of AHSI (B).

A. The case of Menzies

The claimants argued that the GATS MFN clause made it possible to import the consent to arbitration that Senegal had given in the two BITs. Senegal argued, among other things, on the contrary, that the claimants could not invoke the GATS because private individuals cannot invoke WTO agreements.

The tribunal refused to find for the claimants, believing that their argument was based on a “complex and very equivocal mechanism” (para. 131). It invoked three main elements in support of its decision.

1. The GATS does not provide consent to arbitration

According to the tribunal, “there is no consent to arbitration in any form whatsoever in article II of the GATS” (para. 139). Considering that this article refers neither to arbitration nor even to dispute settlement, the tribunal concluded that it could not extract from it the express, clear and unambiguous consent of Senegal

to arbitration for nationals of Luxembourg such as Menzies, as required by general international law and investment arbitration.

2. The MFN clause in article II of the GATS is not applicable to investment arbitration

According to the claimants, as the GATS MFN clause is applicable “to measures [...] that affect trade in services” (para. 115), this would include “offers of consent to arbitration” (para. 117). From this, offers of arbitration contained in the two BITs would be more favourable “treatment” within the meaning of the GATS, to the benefit of services similar to Menzies.

The tribunal was not convinced that article II of the GATS was applicable to investment arbitration. Based on discussions during the GATS negotiations, the tribunal concluded that member states had not given their “informed and unequivocal consent to application of the arbitration clauses contained in BITs” (para. 149). This conclusion was confirmed, said the tribunal, by the subsequent practice of states, which preferred to grant access to international arbitration to service providers in BITs and not through the GATS.

The tribunal also decided that even if it had been shown that article II of the GATS was applicable to investment arbitration, this did not constitute consent to arbitration or the extension of an offer of arbitration. The consequences of a contrary interpretation would be “considerable,” according to the tribunal (para. 145).

3. The claimants invoked BITs made by Senegal with third States for arbitration

According to the claimants, Menzies was entitled to invoke the MFN clause in the GATS to claim access to international arbitration, on the basis of two third-party BITs (Senegal–Netherlands and Senegal–United Kingdom). Indeed, Menzies asked the tribunal to consider the GATS as the “basic treaty” in implementation of the MFN clause, to import the more favourable treatment granted in these two BITs; this more favourable treatment here being the offer of arbitration.

The tribunal dismissed these arguments and refused to “‘compose’ consent by ‘the gluing together’ of disparate parts subsequent to [...] an analysis of the ‘interplay’ between the MFN clause and the offers of arbitration addressed to investors from third States” (para. 135).

B. The case of AHSI

With regard to AHSI, the tribunal upheld the position of Senegal, according to which article 12 of the investment code did not constitute an independent offer of consent to arbitration or a unilateral grant of jurisdiction. It also noted, as affirmed by the respondent, that AHSI, registered in the British Virgin Islands, did not benefit from the protection of the Senegal–United Kingdom BIT. Therefore, AHSI could not invoke the offer of arbitration.

Having accepted Senegal's first objection to jurisdiction, the tribunal decided that it was not necessary to examine the other objections, and it declined jurisdiction to hear the case.

Based on the "costs follow the event" principle, the tribunal decided that the claimants were to bear all the costs of the arbitration and also the costs for legal counsel incurred by Senegal.

Notes: The tribunal was composed of Bernard Hanotiau (President appointed by the parties, Belgian national), Hamid Gharavi (claimants' appointee, Franco-Iranian national), and Pierre Mayer (respondent's appointee, French national). The award is available in French only at <http://www.italaw.com/sites/default/files/case-documents/italaw7483.pdf>. Quotes in this summary were translated from French, unless otherwise indicated.

PCA tribunal deemed acts of Polish agricultural property agency not attributable to Poland

Mr. Kristian Almås and Mr. Geir Almås v. The Republic of Poland, PCA Case No. 2015-13

Claudia María Arietti López

In a case administered by the Permanent Court of Arbitration (PCA), a tribunal decided that the acts of Poland's agricultural property agency were not attributable to Poland, dismissing the case initiated by Norwegian claimants, Kristian Almås and Geir Almås, on its merits.

Factual background and claims

The claimants were the sole shareholders in Pol Farm Sp. z oo (Pol Farm). In 1997 Pol Farm and Poland's agricultural property agency (ANR, in its Polish acronym) entered into a lease of approximately 4200 hectares of land in Świdwin Commune, Poland (Lease Agreement).

After conducting a series of inspections and finding several irregularities in Pol Farm, ANR terminated the Lease Agreement in July 2009. In October 2009, a District Court in Poland opened Pol Farm's bankruptcy proceedings and liquidated the company. In addition, in October 2015, a criminal court in Poland found the claimants guilty of misappropriation and several other charges. The judgment is currently under appeal.

In November 2013, the claimants initiated arbitration against Poland, claiming that ANR's actions breached the Norway–Poland bilateral investment treaty (BIT) by expropriating their investment without adequate compensation, failing to accord them equitable and reasonable treatment and protection, and subjecting them to unreasonable and discriminatory measures. They also argued that Poland's termination of the Lease Agreement breached the BIT's umbrella clause. They requested compensation in the amount of €23 million, in addition to interest and costs. The claimants did not include the criminal convictions against them and the bankruptcy order against Pol Farm in the claim.

Scope of claimants' case determined by issue of attribution of ANR's actions to Poland

The claimants' main claim was that ANR's termination of the Lease Agreement amounted to indirect expropriation. The tribunal thus focused first on whether ANR's conduct could be attributed to Poland, pointing out that the lack of attribution would undermine all claims. As suggested by both parties, the tribunal turned to the International Law Commission's 2001 Draft Articles on Responsibility of States in Internationally Wrongful Acts (the ILC Articles) to analyze the issue.

ILC Article 4: Is ANR a state organ?

ILC Article 4 expresses that the conduct of a state organ—including any person or entity with that status under the domestic law of the state—is considered an act of that state. The tribunal noted that, under Polish domestic law, ANR has separate legal personality and exercises operational autonomy. Accordingly, it concluded that ANR could not be considered a *de jure* state organ under the laws of Poland.

The tribunal also noted that the commentary to ILC Article 4 considers that an entity can also be a *de facto* state organ. In this regard, the claimants argued that ANR exercises executive functions of the state because it has the power to manage, sell and lease state agricultural property. The tribunal disagreed with the claimants' view, considering that an agricultural lease is a commercial transaction, even if entered into with a state entity and even if it involves state-owned land.

Furthermore, to analyze ANR's autonomy, the tribunal looked at two other cases, *Hamester v. Ghana* and *Jan de Nul v. Egypt*. Based on the shared features of the entities in these cases and ANR, the tribunal concluded that ANR could not be considered a *de facto* state organ since it enjoys managerial and financial autonomy.

ILC Article 5: Was the termination of the lease performed in the exercise of governmental functions?

Under ILC Article 5, the conduct of an entity that is not a state organ can still be attributed to a state when that entity can exercise governmental authority and actually exercises that authority when performing the relevant conduct.

When analyzing this article, the tribunal relied on *Jan de Nul's* two-prong test, which states that acts must be carried out by an entity empowered to exercise governmental authority, and the act itself must involve the exercise of that government authority.

The tribunal noted that even though ANR entered into the Lease Agreement by exercising its statutory power to manage the state's agricultural property, it was not exercising a governmental authority when it terminated it. Therefore, it concluded that such action could not be attributed to Poland.

To counteract the above, the claimants argued that the termination was not authorized by the Lease Agreement, and that it was the result of an underlying policy motivation, which converted the act into an exercise of state authority under ILC Article 5.

The tribunal disagreed with the claimants, stating that it did not need to reach a “definitive conclusion as to the lawfulness of ANR’s termination of the Lease Agreement under Polish law” (para. 251). It pointed out that it only needed to decide, as it already had, that the termination was an exercise of a contractual power.

Concerning whether the termination was motivated by an underlying policy, the tribunal analyzed the *Vigotop v. Hungary* award, on which the claimants relied. The *Vigotop* tribunal determined that Hungary expropriated Vigotop’s investment by exercising a termination provision in a contract signed by its subsidiary with Hungary.

The tribunal first noted that the *Vigotop* case concerned the termination of a contract with the state itself and not with a separate entity with contractual capacity. It then analyzed whether the conditions articulated by the *Vigotop* tribunal were satisfied, and concluded that they were not.

ILC Article 8: Was the termination of the lease performed on the instructions of the Polish government?

The tribunal also looked at ILC Article 8, under which the conduct of an entity can be considered an act of a state if the entity is, in fact, acting on the instructions or under the direction or control of that state in carrying out the conduct.

Relying on the commentary to ILC Article 8 and the awards in *Jan de Nul v. Egypt* and *White Industries v. India*, the tribunal indicated that to determine whether the act of an entity could be attributed to a state, the state should have control over both the entity and the specific act in question.

Finding no evidence that ANR acted on the instructions or under the direction or control of the Polish government, the tribunal concluded that there was no basis for attribution under ILC Article 8.

Notes: The tribunal was composed of James R. Crawford (Presiding arbitrator, appointed by his co-arbitrators, Australian national), Ola Mestad (claimant’s appointee, Norwegian national) and August Reinisch (respondent’s appointee, Austrian national). The award dated June 27, 2016 is available at <http://www.pcacases.com/web/sendAttach/1872>.

Claimant not considered investor due to interpretation of “seat” under Cyprus–Montenegro BIT
CEAC Holdings Limited v Montenegro, ICSID Case No. ARB(AF)/14/8
María Florencia Sarmiento

A tribunal at the International Centre for Settlement of Investment Disputes (ICSID) declared by majority that

the claimant did not have a “seat” in Cyprus under the Cyprus–Montenegro bilateral investment treaty (BIT) and therefore did not qualify as an “investor” under the BIT. Accordingly, the tribunal declined to exercise jurisdiction over the case.

Factual background and claims

The case concerns an aluminum plant (KAP) in Montenegro which was owned and managed by CEAC, a company established under the laws of Cyprus. In 2003 CEAC acquired approximately 65 per cent of KAP’s shares from the Government of Montenegro. To improve and make KAP profitable, CEAC also purchased a minority share of KAP’s main supplier of raw materials, RBN. In addition, CEAC’s parent company acquired in a tender process all of the shares in a Montenegro state-owned coal power plant to ensure KAP had a source of electricity.

In 2006 CEAC began experiencing problems when it learned that Montenegro had provided inaccurate financial statements for KAP and RBN during the tender process, which understated KAP’s debts and obligations by €10 million. This led to the end of the privatization of the coal power plant by the Montenegrin parliament “based on dubious reasoning,” compromising KAP’s supply of competitively-priced electricity.

CEAC initiated an arbitration against the sellers and Montenegro under the purchase and sale agreement in order to resolve these issues, but it was discontinued after entering into a settlement agreement in November 2007. Pursuant to the settlement, CEAC transferred 50 per cent of its shares in KAP to Montenegro, which in exchange undertook to subsidize KAP’s electricity supply and to issue state guarantees to KAP.

In 2014, CEAC initiated ICSID arbitration against Montenegro, asserting that the government impeded its attempts to restructure and modernize KAP by a number of actions that caused KAP to default on its debts. These actions included, according to CEAC, the refusal to provide KAP with the electricity subsidies granted under the settlement agreement, the refusal of Montenegro’s representative on the KAP board of directors to approve the financial statements and business plan and the refusal to provide its written consent as guarantor under a loan agreement.

CEAC claimed that Montenegro breached several obligations under the BIT, including the fair and equitable treatment (FET) standard, the national and most-favoured-nation treatment clauses and the prohibition against unlawful expropriation, requesting monetary compensation.

The issue of the “seat”

CEAC sought an award declaring that it had a seat in Cyprus and thus qualified as an “investor” pursuant to Article 1(3)(b) of the BIT. For its part, Montenegro requested a declaration that CEAC did not have a seat in Cyprus.

Article 1 of the BIT provides in relevant part: “3. The term ‘investor’ shall mean [...] (b) a legal entity incorporated, constituted or otherwise duly organized in accordance with the laws and regulations of one Contracting Party, having its seat in the territory of that Contracting Party and making investments in the territory of the other Contracting Party.”

According to CEAC, the meaning of the term “seat” cannot be interpreted autonomously under the treaty but should be determined by a *renvoi* to municipal law. In this context, CEAC maintained that the term “seat” means “registered office,” not “real seat,” and that this is the interpretation supported by Regulation of the European Parliament and the treaty practice of both Cyprus and Montenegro. It contended that it established its registered office in Cyprus and that the respective certificates of registered office constitute conclusive evidence to this effect.

In Montenegro’s view, the “seat” is the place where a legal entity is effectively managed and financially controlled and where it carries out its business activities. It also asserted that the object and purpose of the BIT do not provide a *renvoi* to municipal law because the “seat test” must be conducted on a basis of reciprocal and identical criteria.

According to Montenegro, the term “seat” interpreted autonomously under the BIT required something “more than a registered office” and even under Cypriot law, the term “seat” cannot be considered as a “registered office” (para. XYZ).

Montenegro’s view was that, regardless of the interpretation of the term, CEAC did not have a seat in Cyprus, and the address provided for the alleged office did not qualify as a registered office within the context of Cypriot law. It disputed that the certificates produced were conclusive evidence, indicating that such certificates are issued without any independent investigation. It also asserted that an attempt to courier a package to that CEAC’s address in Cyprus failed three times because CEAC was not known at that address.

The tribunal’s analysis

The majority considered that for purposes of the analysis it was not necessary to determine the precise meaning of the term “seat” as employed in the BIT given that the evidence in the record did not support a finding that CEAC had a registered office in Cyprus at the relevant time.

The majority also considered that, even under Cypriot municipal law, certificates of registered office are not conclusive evidence that the office exists. It noted that CEAC neither provided evidence against Montenegro’s assertions that the office appeared unoccupied and inaccessible to the public nor indicated another address in Cyprus. Therefore, it concluded that CEAC did not have a registered office in Cyprus at the time the request of arbitration was filed.

CEAC had asserted an alternative claim, alleging tax residency in Cyprus, but the tribunal concluded that, under Cypriot law, “seat” cannot be equated with “tax residence.”

Decision and costs

The majority decided that CEAC did not have a “seat” in Cyprus and therefore did not qualify as an “investor” under the BIT. As a consequence, the majority found that it had no jurisdiction to hear the case and dismissed all other claims. It also ordered CEAC to bear the full cost and expenses of the proceedings except the ones incurred regarding Montenegro’s preliminary objections according to the principle that costs should follow the event and given the fact that Montenegro’s preliminary objections were dismissed.

Separate opinion by William Park

William Park, the arbitrator appointed by CEAC, issued a separate opinion dissenting on the central issue of the seat. Park disagreed with the majority’s finding that “seat” requires more than a “registered office”, asserting that the term remains essentially a municipal law concept derived from continental systems. According to the arbitrator, the plain meaning of “registered office” matches the meaning of “seat” in Cyprus as used in the BIT. Under this standard, the Park stressed that CEAC appeared to have a seat.

Notes: The ICSID tribunal was composed by Professor Bernard Hanotiau (President agreed to by the parties, Belgium national), Professor William P. Park (claimant’s appointee, Switzerland and United States national), and Brigitte Stern (respondent’s appointee, French national). The award of July 26, 2016 is available in English only at <http://www.italaw.com/sites/default/files/case-documents/italaw7456.pdf>.

Ecuador’s levy on extraordinary oil profits at a 99% rate has breached Murphy’s legitimate expectations, decides PCA tribunal

Murphy Exploration & Production Company - International v. Republic of Ecuador, PCA Case No. 2012-16 (formerly AA 434)
Inaê Siqueira de Oliveira

In the proceeding brought by U.S.-based company Murphy Exploration & Production Company – International against Ecuador, a tribunal under the auspices of the Permanent Court of Arbitration (PCA) held that Ecuador breached the fair and equitable (FET) treatment under the Ecuador–United States bilateral investment treaty (BIT) by enacting Law 42 and Decree 662, which established a levy on oil profits resulting from sales above a certain reference price.

This was not the first time an arbitral tribunal ruled on a case brought by Murphy against Ecuador. In December 2010, after a proceeding that took nearly 3.5 years, the majority of a tribunal at the Centre for Settlement of Investment Disputes (ICSID) had declined jurisdiction to hear the case (ICSID Case No. ARB/08/4).

The Participation Contract

The starting point of the dispute is a Participation Contract signed in 1996 between *Corporación Estatal Petrolera Ecuatoriana*, the predecessor of the state-owned Petroecuador, and a consortium of foreign investors for oil exploration and production (Consortium). Murphy controlled one of the companies participating in the Consortium until March 2009.

Under the Participation Contract, Consortium members had ownership rights over their shares in oil production. The shares were calculated using a formula, which, according to Murphy, did not include oil price as a variable. According to Ecuador, however, “the price of oil was an integral part of the formula for calculating the parties’ shares in participation” (para. 74).

The global rise in oil prices, Law 42 and Decree 662

In early 2002, global prices of crude oil began to rise, reaching a peak of US\$75 per barrel in July 2006, nearly four times the medium price of the two earlier decades (approx. US\$20 per barrel).

In that scenario, Ecuador enacted Law 42, amending the country’s Hydrocarbons Law to allow “the State to receive from oil companies with participation contracts what was described as ‘participation in the surplus of oil sale prices’” (para. 82). Said differently, Law 42 provided that Ecuador would participate in the Consortium’s extraordinary income resulting from the sale of crude oil *above* the reference price—namely, the oil price that prevailed when the Participation Contract was concluded. Through Law 42 Ecuador set its participation at a minimum of 50 per cent of the extraordinary profits resulting from prices exceeding the reference price; in 2007, through Decree 662, Ecuador changed it to 99 per cent.

Murphy alleged that Law 42 had been a unilateral modification of the Participation Contract and that, because of the law’s detrimental effects on the investment, “it had no choice but to forego its investment by selling its interest in the Consortium” (para. 5). Ecuador, on the other hand, replied that Law 42 was a “matter of taxation” explicitly carved out from the BIT, implemented in view of an exceptional rise in oil prices, and that Law 42 aimed to maintain the agreements with petroleum sector operators while protecting public interest in natural resources.

The tribunal’s jurisdiction: the meaning of “taxation”

Ecuador submitted that Law 42 was a “matter of taxation,” which Article X of the BIT excludes from dispute resolution, unless related to certain specific claims (for instance, expropriation). The tribunal rejected Ecuador’s assertion. Following the approach taken in *EnCana v. Ecuador*, *Occidental v. Ecuador* and *Duke Energy v. Ecuador* for interpreting the meaning of “matter of

taxation,” the tribunal considered it necessary to assess “whether that measure comes within the State’s domestic tax regime” (para. 166) and whether the measure could be characterized as tax at international law.

According to the tribunal, Law 42, unlike the challenged measure in *EnCana*, was “not enacted as a tax or otherwise part of the national tax regime” (para. 175), but enacted as an amendment to the Hydrocarbons Law under the President’s power to submit emergency draft legislation. Relying on *Burlington v. Ecuador*, the first tribunal to rule on whether Law 42 was a tax-related measure, and *Occidental II v. Ecuador*, which also analyzed the issue, the tribunal held that Law 42 did not constitute a matter of taxation within the meaning of the BIT. It considered the measure “a unilateral change by the State to the terms of the participation contracts that were governed by the Hydrocarbons Law” (para. 190).

The breach of FET

As for the merits of the dispute, the tribunal did analyze whether the FET provision of the BIT reflected an autonomous standard above the customary international law one. Instead, it considered “that there is no material difference” (para. 208) between them and proceeded to the analysis of whether Law 42 and Decree 662 breached Murphy’s legitimate expectations.

The tribunal accepted the notion, suggested by Murphy, that legitimate expectations “are grounded in the legal framework as it existed at the time that the investment was made” (para. 249). Thus, it considered that Murphy could legitimately expect that the terms of the Participation Contract would not change and that changes would only be made “within the confines of the law and pursuant to a negotiated mutual agreement between the contractual partners” (para. 273).

The tribunal disagreed with Murphy’s assertion that the Participation Contract contained a stabilization clause, which would prevent regulatory and legislative adjustments even in exceptional circumstances, such as a significant rise in oil prices. It found that Law 42, not having altered the Participation Contract in a fundamental way, had not breached Murphy’s legitimate expectations.

The tribunal did, however, find that Decree 662, which raised the state’s participation in the extraordinary income to 99 per cent, breached Murphy’s legitimate expectations. In the tribunal’s understanding, Decree 662 transformed the Participation Contract in a service contract, changing “the foundational premise upon which the Participation Contract had been agreed” (para. 282), namely, the Consortium’s ability to participate in the upside of high oil prices. It also referred to the “hostile and coercive investment environment” (para. 281) prevailing when Decree 662 was adopted as an element that reinforced the conclusion that Ecuador had breached its FET obligation.

The tribunal condemned Ecuador to pay nearly US\$20 million in compensation to Murphy for damages incurred as a result of the payments, plus pre-award (approx. US\$7.2 million) and post-award interest.

It also ordered Ecuador to pay the difference between the price at which Murphy was sold in 2009 (US\$78.9 million) and the company's fair market value as if Murphy had continued to make payments under Law 42 at 50 per cent, plus interest. If the parties do not agree on the latter value within three months, "the Tribunal will then make the necessary findings" (para. 504).

Notes: The arbitral tribunal was composed of Bernard Hanotiau (President appointed by the co-arbitrators), Kaj Hobér (Claimant's appointee), and Yves Derains (Respondent's appointee, appointed following the resignation of Georges Abi-Saab in December 2013). The award of May 6, 2016 is available at http://www.italaw.com/sites/default/files/case-documents/italaw7489_0.pdf

Ecuador ordered by PCA tribunal to pay \$24 million to Canadian mining company

Copper Mesa Mining Corporation v. Republic of Ecuador, PCA No. 2012-2

Matthew Levine

A tribunal under the auspices of the Permanent Court of Arbitration (PCA) constituted under the Canada–Ecuador Agreement for the Promotion and Reciprocal Protection of Investments (FIPA) has reached the award stage.

The tribunal ordered Ecuador to compensate a Canadian company for expropriation of two mineral concessions. The alleged expropriation of the company's option interest in a third concession was dismissed. In light of contributory negligence by the company's executives, the tribunal discounted damages by 30 per cent. The parties were ordered to bear their own legal costs and to share arbitration costs equally.

Background and claims

Between 1991 and 1997, the first sophisticated geological tests were conducted in the Junín area of Northwestern Ecuador. The final technical report confirmed large deposits of copper and noted potential environmental impacts of a proposed mine. Since then, an increasing number of local residents concerned about the deleterious impacts of mining organized to resist the activity.

Even so, in December 2002 Ecuador granted the Junín concession to an Ecuadorian national. In 2005, Canadian company Copper Mesa Mining Corporation Exploration (Copper Mesa), through Barbadian and Ecuadorian subsidiaries, acquired the Junín concession, the neighbouring Chaucha concession and an option for the Telimbela concession.

From 2005 onwards, Copper Mesa made a series of expenditures in relation to the concessions. In

particular, it commissioned a geological report, acquired a neighboring concession and surface land in and around the concession areas, prepared and submitted an environmental impact study (EIS) for the exploration phase, employed a team of Ecuadorian staff and committed resources to providing social services and community development.

In April 2008 Ecuador's Constituent Assembly passed legislation known as the Mining Mandate, which declared that mineral substances were "to be exploited to suit national interests" and provided for the termination "without economic compensation" of mining concessions falling into a number of categories (para. 1.110). Ultimately, Ecuador's Under-Secretary of Mines ordered the termination of the Junín and Chaucha concessions due to a lack of prior consultation with the local residents.

In July 2010 Copper Mesa sent a written Notice of Dispute to Ecuador under the Canada–Ecuador FIPA, alleging that Ecuador unlawfully revoked or terminated the concessions, thereby depriving it the entire value of its investments and causing it to suffer substantial damages.

Investor is entitled to advance own claims in relation to inter-company loans to affected subsidiaries

Ecuador objected to the tribunal's jurisdiction over all of Copper Mesa's claims. In regard to the Junín concession, Ecuador also objected to the admissibility of the claims.

In an important objection to jurisdiction, Ecuador argued that Copper Mesa's claim concerning damages to its local subsidiaries must be distinguished from a claim on its own behalf, and that the local subsidiaries must have separately consented to arbitration and waived any rights each may have under Ecuadorian law. However, the tribunal agreed with Copper Mesa that the company had complied with the formal requirements for initiating arbitration. It held that Copper Mesa was entitled, as a matter of jurisdiction and admissibility, to advance its own claims against the respondent, in respect of its own investments in Ecuador. According to the tribunal, the claimant was not seeking to advance or espouse any claim in the name of any its subsidiaries; it was only claiming compensation for harm that it itself had suffered.

The tribunal also addressed Ecuador's contention that Copper Mesa had "unclean hands." For the tribunal, Ecuador had adduced an impressive amount of expert testimony and materials relating to the legal doctrine of unclean hands under international law, including the obligations of foreign investors on human rights in the broadest sense. Even so, the tribunal indicated that this was a matter of admissibility rather than jurisdiction, and that Ecuador had not made a single complaint as regards international law, international public policy or human rights to the claimant prior to the commencement of arbitration. For the tribunal, it was then much too late.

Tribunal reconciles unlawful expropriation and FIPA's General Exception provision

Copper Mesa's substantive claims included Ecuador's obligations to pay compensation upon direct or indirect expropriation, to provide fair and equitable treatment and full protection and security, and to provide national treatment.

With regards to expropriation, Ecuador contended that the Mining Mandate was a measure issued by the state in exercise of its legitimate regulatory authority and responding to a compelling public policy consideration, that is, the need to consult the affected local population, and seeking to address many unsolved social, economic and environmental issues. For Ecuador, the Mining Mandate therefore fell under the FIPA's General Exceptions provision.

In the tribunal's view, the applicable legal standards under international law were not in doubt. Rather, the primary issue was whether, in the circumstances, the government had acted in accordance with due process and not in an arbitrary manner. In particular, the tribunal sought to emphasize that its inquiry stemmed not from the Mining Mandate itself but from the Termination Resolutions ordered by the Under-Secretary of Mines based on the Mining Mandate.

Given the particular circumstances of the Termination Resolutions, the tribunal decided that they were "no mere regulatory measures, because, in the circumstances, these Resolutions were made in an arbitrary manner and without due process," (para. 6.66) and held that "the permanent taking of the Claimant's Junín concessions was an expropriation" under the FIPA (para. 6.67).

Damages reduced to reflect claimant's contributory negligence

Copper Mesa had sought in its primary case on quantum to have the tribunal ratify a market-based quantification of damages with the mid-point of the relevant range falling at US\$69.7 million. In the alternative, it presented a cost-based quantification amounting to US\$26.5 million, as confirmed by its audited financial statements.

The tribunal began its analysis with the general principle under international law that it is for the claimant to prove the extent of its injury. It found that, ultimately, the market-based quantification relied on a methodology that was too uncertain, subjective and dependent upon contingencies. According to the tribunal, the "most reliable, objective and fair method in this case for valuing the Claimant's investments in November 2008 and June 2009 is to take the Claimant's proven expenditure incurred in relation to its Junín and Chaucha concessions" (para. 7.27).

With regards to the Junín concession, the tribunal decided that Copper Mesa contributed to 30 per cent of its loss by negligent acts and omissions committed

by its own senior management in Canada. After deduction of such 30 per cent, the net loss on the Junín concession was set at US\$11,184,595.80.

For the Chaucha concession, contributory negligence was not an issue, and Copper Mesa was awarded \$8.3 million plus compound interest. For the claim related to Copper Mesa's option on Telimbela having been dismissed, no damages were awarded.

Local residents sought to "countersue" Copper Mesa in Canadian courts

The Junín concession was located adjacent to a series of small villages. Between December 2005 and July 2007, tensions between village residents and Copper Mesa exploded into a series of physical confrontations.

In 2009 certain village residents filed a claim in Ontario courts against Copper Mesa and various other Canadian persons. In that lawsuit, the village residents claimed to have been subjected to a "campaign of intimidation, harassment, threats and violence" by security forces and other agents of Copper Mesa (OCA Judgment, para. 11). The court however found that, as the claims against Copper Mesa were based solely on vicarious liability, they disclosed no reasonable cause of action under the applicable Canadian law.

Subsequently, the Ontario Court of Appeal dismissed the village residents' appeal. In doing so, it found: "The threats and assaults alleged by the plaintiffs are serious wrongs. Nothing in these reasons should be taken as undermining the plaintiffs' rights to seek appropriate redress for those wrongs, assuming that they are proven. But that redress must be sought against proper parties, based on properly pleaded and sustainable causes of action. The claims at issue in these proceedings do not fall in that category" (OCA Judgment, para. 99).

Notes: The tribunal was composed of V.V. Veeder (President appointed by party agreement, British national), Bernardo Cremades (claimant's appointee, Spanish national), and Bruno Simma (respondent's appointee, German national). The final PCA award of March 15, 2016 is available at <http://www.italaw.com/sites/default/files/case-documents/italaw7443.pdf>. The Ontario Court of Appeal's judgment in *Piedra v. Copper Mesa Mining Corporation*, 2011 ONCA 191, is available at <http://www.ontariocourts.ca/decisions/2011/2011ONCA0191.pdf>.

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resources and events

Resources

Judging the State in International Trade and Investment Law

By *Leïla Choukroune (Ed.)*, Published by Springer, November 2016

The book analyzes the particularities of statehood and the limitations of the dispute settlement systems to judge sovereign states. Questionable professionalism, independence and impartiality of adjudicators, as well as a lack of consistency of decisions challenging public policies, have all contributed to the controversy surrounding trade and investment disputes. These challenges call for a rethinking of why, how and what for states are judged. The book covers issues such as global judicial capacity-building and judicial professionalism from an international and domestic comparative angle, states' legitimate right to regulate, legal challenges of being a state claimant, uses and misuses of imported legal concepts and principles in multidisciplinary adjudications, and the need to reunify international law on a (human) rights-based approach. Available at <http://www.springer.com/gp/book/9789811023583>

Interpretation of International Investment Treaties

By *Tarcisio Gazzini*, Published by Hart Publishing, November 2016

Most investment treaty claims have raised and continue to raise crucial and often complex issues of interpretation. Fundamental questions dealt with in this study include: Are investment treaties a special category of treaty for the purpose of interpretation? How have the rules on interpretation contained in the Vienna Convention on the Law of Treaties (VCLT) been applied in investment disputes? Have tribunals developed new techniques concerning treaty interpretation and, if so, are they consistent with the VCLT? How can interpretation problems be solved or minimized? How creative have tribunals been in interpreting investment treaties? Are states capable of keeping effective control over interpretation? Available at <http://www.bloomsburyprofessional.com/uk/interpretation-of-international-investment-treaties-9781849462686>

Mining a Mirage? Reassessing the shared-value paradigm in light of the technological advances in the mining sector

By *Aaron Cosbey, Howard Mann, Nicolas Maennling, Perrine Toledano, Jeff Geipel & Martin Dietrich Brauch*, Published by IISD, October 2016

This report, co-produced with the Columbia Center on Sustainable Investment, looks to the near and medium terms, exploring what will happen to the local employment and procurement components of the shared-value paradigm—and, by extension, to the mining companies' social licence to operate—if technological change radically alters the amount of money mining firms are spending on hiring and procurement. It surveys the trends in technology development, and uses procurement and other data from two global mining firms to estimate the types of impacts we might see. It concludes by exploring the ways in which governments and firms might address the predicted results. Available at <http://www.iisd.org/library/mining-mirage-reassessing-shared-value-paradigm-light-technological-advances-mining-sector>

Investment-Related Dispute Settlement: Towards an inclusive multilateral approach

By *IISD Investment and Sustainable Development Program*, Published by IISD, October 2016

In 2014, IISD convened an expert meeting to explore alternative models for settling investment disputes at the international level to supplement or replace existing mechanisms. Building on the results of the 2014 meeting and recent developments in international practice regarding investment-related dispute settlement, IISD prepared a preliminary draft outline of an Agreement Creating an International Dispute Settlement Agency for Transboundary and Other Investments, which was the main subject of

the discussions at the second expert meeting in Montreux held from May 23 to 24, 2016. Experts considered and critiqued elements of the draft outline, suggested alternative approaches and identified additional resources and sources to consider. Participants also discussed institutional and strategic options for further development of an institutional basis for an expanded international regime for the resolution of investment disputes. Available at <http://www.iisd.org/library/investment-related-dispute-settlement-towards-inclusive-multilateral-approach>

Ending Hunger: What would it cost?

By *David Laborde, Livia Bizikova, Tess Lallemand & Carin Smaller*, Published by IISD, October 2016

IISD and the International Food Policy Research Institute joined forces to estimate what it would cost to end hunger, and the contribution that donors need to make. The analysis focuses on the cost of ending hunger through increased spending on social safety nets directly targeting consumers, farm support to expand production and increase poor farmers' income, and rural development that reduces inefficiencies along the value chain and enhances rural productivity. The research marks the first time that a multi-country macroeconomic model has been combined with household surveys. The authors found that it will cost on average an extra US\$11 billion per year of public spending from now to 2030 to end hunger. US\$4 billion of the additional spending needs to come from donors. The remaining US\$7 billion will come from poor countries themselves. Importantly, this public spending will generate on average an additional US\$5 billion of private investment per year until 2030. Available at <http://www.iisd.org/library/ending-hunger-what-would-it-cost>

Events 2016–2017

November 28–December 9, 2016

2016 INTERNATIONAL INVESTMENT TREATIES AND INVESTOR–STATE ARBITRATION, International Law Institute, Washington, DC, United States, <http://www.ili.org/training/ili-brochure/upcoming-programs-and-events/624-2016-international-investment-treaties-and-investor-state-arbitration.html>

December 7–9, 2016

INTRODUCTION TO MEDIATION, Association for International Arbitration, Brussels, Belgium, <http://www.arbitration-adr.org/activities/?p=conference&a=upcoming>

December 9, 2016

33rd AAA–ICC–ICSID Joint Colloquium on International Arbitration, ICC, American Arbitration Association (AAA) & International Centre for Settlement of Investment Disputes (ICSID), Paris, France, <http://www.iccwbo.org/Training-and-Events/All-events/Events/2016/33rd-AAA-ICC-ICSID-Joint-Colloquium-on-International-Arbitration>

ROUNDTABLE ON CORPORATE LIABILITY FOR FOREIGN

BRIBERY, Organisation for Economic Co-operation and Development (OECD), Paris, France, <http://www.oecd.org/corruption/roundtable-on-corporate-liability-for-foreign-bribery.htm>

January 12–13, 2017

4TH ITA–IEL–ICC JOINT CONFERENCE ON INTERNATIONAL ENERGY ARBITRATION, ICC, Institute for Transnational Arbitration (ITA) & Institute for Energy Law (IEL), Houston, Texas, <http://www.iccwbo.org/Training-and-Events/All-events/Events/2017/4th-ITA-IEL-ICC-Joint-Conference-on-International-Energy-Arbitration>

January 17–20, 2017

WORLD ECONOMIC FORUM ANNUAL MEETING, Davos-Klosters, Switzerland, <https://www.weforum.org/events/world-economic-forum-annual-meeting-2017>



Investment Treaty News Quarterly is published by the International Institute for Sustainable Development. The views expressed in this publication do not necessarily reflect those of the IISD or its funders, nor should they be attributed to them.

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